

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

Apple Canyon Utility Company)	
)	
Proposed general increase in water rates)	Docket No. 12-0603
)	
Lake Wildwood Utilities Corporation)	
)	
Proposed general increase in water rates)	Docket No. 12-0604
)	

REPLY BRIEF OF
THE PEOPLE OF THE STATE OF ILLINOIS

The People of the State of Illinois

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Table of Contents

I.	Introduction	1
II.	Appeals Costs	2
III.	Survey Costs.....	3
	A. Leak Surveys	4
	B. Service Area Boundary Surveys	5
IV.	Cash Working Capital	5
V.	Pro Forma Plant Additions	6
	A. Tank Painting.....	6
	B. Well #1.....	7
	C. Water Treatment Project.....	8
VI.	Conclusion.....	8

The People of the State of Illinois, by LISA MADIGAN, Attorney General of the State of Illinois (the “People,” or “AG”), pursuant to the Commission’s rules, 83 Ill. Admin. Code 200.800, file their Reply Brief in response to the Initial Briefs of Apple Canyon Utility Company (“Apple Canyon”) and Lake Wildwood Utilities Corporation (“Lake Wildwood”) (jointly “the Companies”) and Commission Staff in connection with the Companies’ request for a substantial increase in revenues for water service for customers in Illinois.

I. Introduction

As demonstrated in the People’s Initial Brief, the public comments in this case demonstrate a level of outrage directed at the Companies ranging from issues such as the quality of the water, which has been described as “like an oil spill,” to the quality of service, which involved Company personnel telling customers that “they were not our water company.”¹ While providing a level of service that results in this publicly available list of complaints, the Companies, in their Initial Brief, simultaneously complain that they do not receive a sufficient level of revenue.

The People urge the Commission to remain cognizant of these public comments when reviewing the remaining unresolved issues in this case. First, as to the recovery of appeals costs, the Companies failed to point to record evidence or any legal authority that would allow recovery for non-recurring costs associated with appeals that the Companies *elected* to make. Next, the Companies did not justify their request to capitalize costs associated with leak surveys and service area boundary surveys. Similarly, the Companies have not countered the People’s proposed reduction to Cash Working Capital. Finally, as to the pro forma plant additions, the Companies failed to justify their requests to recover over \$200,000 for tank painting, well

¹ AG Initial Brief (IB) at 2-3; ICC Docket 12-0604, Public Comments, available at: <http://www.icc.illinois.gov/docket/PublicComments.aspx?no=12-0604> (last accessed May 16, 2013).

repairs, and an addition to a water treatment plant. Therefore, the People urge the Commission to adopt the arguments and proposed adjustments presented herein and in the People's Initial Brief.

II. Appeals Costs

The Companies, in their Initial Brief, fail to justify why they should recover over \$40,000 of non-recurring costs associated with appeals that the Companies *elected* to make. While the Companies incurred and paid these costs prior to the end of the test year, they are non-recurring costs. AG IB at 23. Instead of recognizing that these are non-recurring costs in their Initial Brief, however, the Companies rely on a public interest argument that, generally, appeals are “a valid and reasonable exercise of a right provided by the legislature to defend the Companies’ position.” Companies IB at 4. The Companies’ right to appeal does not justify what is essentially an effort to increase rate case expense after the fact. The People, therefore, stand on the argument presented in their Initial Brief that the Companies provided no evidence demonstrating that the appeal costs reflect annual recurring costs and reiterate that these costs should not be included in rate base. AG IB at 23-24. Moreover, the Companies’ assertion that the appellate case in question involved only defensive work is patently wrong, as the record clearly demonstrates that the Companies’ cross-appeal raised new issues and, therefore, the Companies were not simply defending their position.

The Companies also fail to cite authority to support their public interest argument that they have a “right” to appeal. Somehow, according to the Companies, disallowing recovery impacts their right to file an appeal. The People simply respond that the Companies are free to appeal whichever Commission decisions they deem as appropriate. However, as demonstrated in the People’s, Staff’s and the Associations’ Initial Briefs, the Companies do not have the right to

recover the costs associated with these appeals in subsequent rate cases. AG IB at 24-25; Staff IB at 14-16. The Companies' argument also wholly ignores a key piece of record evidence. The Companies state that they "did not initiate the appellate review." Companies IB at 5. However, the Companies *did* initiate the cross-appeals in this case. As explained in greater detail in the AG Initial Brief, the issues appealed by Intervenors in the appellate case were different from those appealed by the Companies. AG IB at 24. The Companies point to no precedent that would allow for the Companies to recover from ratepayers the costs of an appeal initiated by a utility. As Commission Staff noted,

If appeals costs are allowed to be recovered from ratepayers, then utilities will have no reason to weigh these costs and benefits with the likelihood of success of the appeal. This could presumably result in an appeal for every Commission decision with which utilities disagree.

Staff IB at 16. The Companies claim that they "could not have included these costs in the rate case expense because it was not known whether the Intervenors would appeal until after the Commission entered the final order." Companies IB at 3. However, the timing of the appeal is of no issue in this case, as noted particularly by Staff Witness Bridal. Staff Ex. 9.0 at 5. The Companies cannot overcome their failure to provide record evidence or legal authority to support their position. AG IB at 23-25. Therefore, the only equitable solution is to disallow these non-recurring costs and save the Apple Canyon and Lake Wildwood ratepayers almost \$40,000.

III. Survey Costs

Next, the Companies failed to provide a record to support including, in test year plant in service, the costs associated with a leak survey and service area boundary surveys. The Companies, without explanation, booked the costs of these surveys as capital expenditures, saddling ratepayers with additional plant in service and depreciation expenses. AG IB at 16-17. The Companies claim that the leak surveys were "instrumental" in order to identify capital

upgrades. Companies IB at 6. However, as was discussed in greater detail in the People’s Initial Brief, an ordinary expense cannot be capitalized if it is not “tied to” a capital expenditure. AG IB at 16-17. Finally, Commission Staff agrees with the People’s adjustment disallowing the survey costs and, like the People, concludes that the Companies have failed to support their position to turn an expense into a rate base item. Staff IB at 5-6.

A. Leak Surveys

As demonstrated in the People’s Initial Brief, the Company did not produce evidence to show that the leak survey was “tied to” a capital asset – therefore under accounting principles, the costs of the survey should have been expensed in the period incurred, rather than capitalized on the books as a capital asset. AG IB 17. The Companies proclaim in their Initial Brief that “Although the Company did not provide a list of the capital assets identified or ‘tied to’ the leak survey, the capital investments necessary to extend the life of these assets actually occurred.” Companies IB at 7. The first half of this statement is critical, in that the Companies admit that they failed to provide record evidence to show that the surveys were “tied to” a capital project. Despite this admission, however, in the second half of the statement, the Companies seem to ask the Commission and Intervenors to merely take their word for it that these investments “actually occurred.” Whether or not these investments actually occurred is irrelevant, particularly where the record evidence proves that the survey was not tied to a capital expense or project. The Companies also rely upon the notion of a “general ledger addition” to support their position. As noted in the People’s Initial Brief, however, this “general ledger” argument reflects an arbitrariness and a failure to follow proper accounting procedures. AG IB at 18. Therefore, the Commission should reject the Companies unjustified and unexplained request to capitalize the costs of the leak survey as recommended by the People and Staff.

B. Service Area Boundary Surveys

Similarly, as to the costs for the service area boundary surveys, the Companies claim that the surveys “were used to expand the respective Companies’ service areas” and should be treated as a capital expenditure. Companies IB at 8. The record evidence, as well as the testimony of Ms. Ramas, however, demonstrates that the surveys of the service areas were not associated with any specific capital additions or capital projects. AG IB at 18. In fact, the surveys were conducted in order to ensure the Companies’ Certificated Area of Convenience for Service was up to date. AG IB at 18. At the evidentiary hearing, the Companies’ own witness admitted that the expansion projects that the Companies now claim to be a result of the surveys could not have been connected to these surveys because the projects happened prior to the surveys. AG IB at 19; Tr. at 67-68. The Companies placed the expenses in the accounting category of “Structures and Improvements.” However, the Companies witness admitted he was unsure how the surveys would classify as either a structure or an improvement. AG IB at 19; Tr. at 66. The evidence does not support the Companies’ position that the service area boundary surveys were done in support of a capital project. Considering the lack of support in the record for the Companies’ position and the fact that a survey is ordinarily an expense, the People urge the Commission to follow the recommendation of the People and Staff to remove the costs of the surveys from rate base.

IV. Cash Working Capital

The People’s Initial Brief and the testimony of regulatory accounting expert Donna Ramas contain details as to the People’s equitable recommendation as to the cash working capital calculation. AG IB at 19-22. In summary, the People’s adjustment should be adopted because it reflects the reality associated with the Companies’ adoption of the 1/8th method to

calculate cash working capital – that *all* taxes other than income should be removed. AG IB at 20. The Companies’ position leaves certain tax expenses, including Illinois Invested Capital Tax, in the calculation. In addition, the People’s calculation removes certain tax expenses that are prepaid. This is an important feature of the People’s adjustment because, as the Companies have acknowledged, prepaid taxes should be booked in the year in which the prepayments are made. AG IB at 22. When an item is prepaid, there is no need for it to be calculated into the daily cash flow needs of the Companies in subsequent years. See AG IB at 21-22.

The People’s adjustment ensures that cash working capital is properly calculated and includes the removal of expenses necessary to reflect any additional adjustments approved by the Commission that could impact maintenance and general expenses. *Id.* Finally, the People’s adjustment, unlike that of the Companies, follows applicable accounting regulations. *Id.* at 22. Considering the facts of the case before us, the Commission should reject the Companies’ proposal to include additional tax expenses other than income and should require the Company to appropriately account for prepaid taxes in their cash working capital calculation. AG IB at 19-20.

V. Pro Forma Plant Additions

A. Tank Painting

As to the tank painting, the Companies claim that their treatment of the tank painting is consistent with past policy. Companies IB at 10. Commission Staff, without adequate explanation, accepts the Companies requests to recover \$100,000 to paint the tank. As demonstrated in the People’s Initial Brief, the Companies have provided no reason to support this *need* to prematurely paint the tower *now* and Commission Staff has presented no justification to accept this request. AG IB at 8. The Companies claim that management determined that the

condition of the tank warranted spending the money to paint the tank and that it should be completed by May 2013. Companies IB at 9.

The Companies provided no proof, however, that the tank needed to be painted at this time. The paint, by the Companies' own admission, should have lasted 10 years. AG Cross Ex. 5. The tower was last painted about 8 years ago. AG Cross Ex. 5. Although the Companies assert this was a "management decision," the record is devoid of any evidence showing the rationale behind that management decision. AG IB at 8. The only evidence is the bids for the project: there are no inspection reports nor are there photographs of the tank. The record does not even contain a final invoice showing the final cost of this project, despite being requested by the Intervenors in this case. Moreover, the record reflects the rushed nature of this project, where a certain project bidder was not able to perform the job because of its rushed nature. AG/ACLPOA/LWA Ex. 2.0 at 12. Absent justification for the management decision to prematurely paint the tank, the Commission should not allow this expense before the useful life of the paint has expired.

B. Well #1

As to the construction project involving Well #1, the People stand on the arguments made in their Initial Brief. The record evidence also shows that the Companies received bids for this project months before rebuttal testimony was filed – yet Staff and Intervenors did not learn of this project until rebuttal testimony. AG IB at 13. In March, there were no contracts or other authorization in place to conduct the project. *Id.* About a month later, however, the Companies witness testified that the project was complete. *Id.* At the evidentiary hearing, however, no one from the Company could pinpoint *when* the project was completed or produce a final invoice.

Id. As demonstrated in the People’s Initial Brief, the Company failed to meet its burden of showing that ratepayers should be burdened with the costs of this project.

C. Water Treatment Project

Similar to Well #1, the Companies knew about this project at the time direct testimony was filed, yet failed to inform Staff and Intervenors of the project until the day before the Companies filed their rebuttal testimony. AG Cross Ex. 1; AG IB at 13. In fact, the Companies knew this project was necessary two years prior to filing the rate case. Utilities Ex. 2.3. Despite having years of advance knowledge, the Companies failed to obtain a bid until just before the Companies filed their rebuttal testimony. In fact, it was then rushed to the point of not being able to seek proposals from certain vendors. AG/ACLPOA/LWA Ex. 2.0 at 7; AG IB at 15. When bids were finally assembled, the project was conducted in the same fast fashion as the Well #1 project. AG IB at 14. As with Well #1, the Companies cite to “management” decisions for the timing issues associated with this project. AG IB at 15. However, the Companies offered no evidence to discuss the rationale behind these management decisions. AG IB at 16; Tr. at 73. The project, at this point, is supposedly complete. However, the People note that there are credibility issues with the testimony of the Companies’ witnesses, who were unable to provide exact completion dates for the project or provide a final invoice for the project. Tr. at 73. As demonstrated in the People’s Initial Brief, the Company failed to meet its burden of showing that ratepayers should be burdened with the costs of this project.

VI. Conclusion

The People respectfully request that the Commission adopt the arguments presented in the People’s Initial and Reply Briefs and reject the Companies’ requested increases in revenue for the pro forma plant additions for Apple Canyon’s water tower painting, Well #1 equipment

replacement and Lake Wildwood's water treatment plant repairs; remove the survey costs from plant in service for Apple Canyon's leak survey and both Companies' service area boundary surveys; reject the Companies' request to recover appeals costs; and adjust the calculation to cash working capital.

Respectfully submitted,

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